

**IT 00-9**

**Tax Type: Income Tax**

**Issue: Net Operating Loss (General)**

**STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
CHICAGO, ILLINOIS**

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**THE DEPARTMENT OF REVENUE  
OF THE STATE OF ILLINOIS**

v.

**“THE DEVONSHIRE COMPANY”,  
TAXPAYER**

**NO. 97-IT-0000  
FEIN: 00-0000000  
TAX YEAR: 9/92**

**KENNETH GALVIN  
ADMINISTRATIVE LAW JUDGE**

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**RECOMMENDATION FOR DISPOSITION**

**APPEARANCES:** Mr. Richard Finn, *pro se*, for “The Devonshire Company”, Mr. Sean Cullinan, appearing on behalf of The Department of Revenue of the State of Illinois.

**SYNOPSIS:**

The Illinois Department of Revenue (hereinafter the “Department”) issued a Notice of Deficiency (hereinafter “NOD”) to “The Devonshire Company” (hereinafter “taxpayer”) on October 30, 1997. The taxpayer filed a timely protest of the NOD and requested a hearing. The basis of the NOD was the Department’s determination that the taxpayer had failed to file an IL-1120 for tax year ending September, 1992, before filing an IL-1120X for that year. Additionally, taxpayer carried back a net loss deduction from the September, 1994, return to the September, 1992, IL-1120X, when taxpayer had already elected to carry this loss forward on its September, 1995 return. A hearing was held on this matter on March 3, 2000, with accountant, “John Doe”,

testifying for the taxpayer and Dwain Hampton, auditor, testifying for the Department. Following submission of all evidence and a careful review of the record, it is recommended that the NOD be finalized as issued. In support thereof, the following “Findings of Fact” and “Conclusions of Law” are made.

**FINDINGS OF FACT:**

1. The Department’s *prima facie* case, inclusive of all jurisdictional elements, was established by the NOD issued on October 30, 1997. The NOD, for tax year ending September, 1992, assessed an underpayment of taxes of \$1,743, Section 1001 penalties of \$654, Section 1005 penalties of \$510, Section 804 penalties of \$105, and interest through October 30, 1997, of \$739. Dept. Ex. No. 1.
2. On November 18, 1997, taxpayers protested the NOD, and requested a hearing. Dept. Ex. No. 3.
3. Taxpayer’s IL-1120 for September, 1994, was originally filed on May 9, 1995. On March 6, 1996, Taxpayer filed an amended U.S. Corporation Income Tax Return for September, 1994, reflecting a net loss of \$298,797. Taxpayer filed an IL-1120-X for September, 1994, on August 15, 1996. Tr. p. 13; Dept. Ex. No. 3.
4. On March 5, 1996, taxpayer filed an IL-1120 for tax year ending September, 1995. Attached to the IL-1120 was a “Schedule NLD Illinois Net Loss Deduction” showing a net loss for tax year ending September, 1994, of \$298,797, and a carry-forward of \$13,480 to tax year ending September, 1995. Tr. p. 12; Dept. Ex. No. 4.
5. On March 5, 1996, when the IL-1120 for September, 1995, was filed and the carry-forward of \$13,480 was utilized, the September, 1994, federal amendment had not yet been finalized. On

May 21, 1996, the U.S issued a refund check for \$4814.09 based on the amended September, 1994, return. Tr. pp. 13-14; Dept. Ex. No. 6.

6. On August 5, 1996, taxpayer filed IL-1120X forms for tax years ending September, 1991, 1992, and 1993, carrying back the year ending September, 1994, net loss deduction in the amounts of \$11,149, \$25,264 and \$4,614, respectively. On May 30, 1997, the Department issued a “Notice of Denial” of taxpayer’s claim for a refund for tax year 1992, and refused to process the IL-1120-X for 1992, because the Department had not received an IL-1120 for that year. Tr. pp. 12-13; Dept. Ex. Nos. 2 and 3.

### **CONCLUSIONS OF LAW:**

Pursuant to Illinois statute, the NOD is *prima facie* correct and is *prima facie* evidence of the correctness of the amount of tax due, as shown therein. 35 ILCS 5/904. In order to overcome this presumption of validity, the taxpayer must produce competent evidence identified with its books and records showing that the NOD is incorrect. Oral testimony is not sufficient to overcome the *prima facie* correctness of the Department’s determinations. A.R.Barnes & Co. v. Department of Revenue, 173 Ill. App. 3d 826 (1<sup>st</sup> Dist. 1988).

In the instant case, the NOD states that the taxpayer failed to file an IL-1120 for tax year ending September, 1992, as required by Sections 501 and 502 of the Illinois Income Tax Act. 35 ILCS 5/501 and 5/502. The Department’s auditor testified that the Department had not received an IL-1120 from the taxpayer for tax year 1992. Tr. p. 11. The auditor also testified that the Department had no record of any payment being made towards the tax due for 1992. Tr. pp. 22-23. The taxpayer’s accountant maintained that the 1992 return was timely filed and that a copy of the 1992 return was included with the 1992 amended return. Taxpayer’s accountant did not have a signed copy of the return and his office did not have a signed copy. Tr. p. 36. The accountant was

asked if he had a copy of a cancelled check showing that there was a payment made for tax year ending 1992. He responded “no.” Tr. p. 39. Based on the Department auditor’s testimony and the taxpayer’s failure to provide any documentary evidence on this issue, I must conclude that the taxpayer has failed to rebut the Department’s *prima facie* case, and that an IL-1120 for tax year 1992 was not filed by the taxpayer.

Because an IL-1120 was not filed for tax year 1992, the taxpayer cannot carry the 1994 loss back to tax year 1992. The carryback of the 1994 loss to tax year 1992 would, if allowed, entitle the taxpayer to a refund. 86 Ill. Adm. Code § 100.9400(f) states that “[a] claim for refund of an overpayment of income tax may be filed with the Department only if a return for the taxable year for which the refund is claimed has been filed.” Accordingly, since no tax return was filed for 1992, the taxpayer cannot claim a refund by carrying back the 1994 loss to that year.

When an Illinois taxpayer’s net income results in a loss, “the loss shall be allowed as a carryover or carryback deduction in the manner allowed under Section 172 of the Internal Revenue Code.” 35 ILCS 5/207. Section 172 of the Internal Revenue Code allows a net operating loss to be carried back to each of the three taxable years preceding the taxable year of the loss, and carried forward to each of the fifteen taxable years following the taxable year of the loss. 26 U.S.C.A. § 172(b)(1). “Any taxpayer entitled to a net loss carryback may elect to relinquish the entire carryback period with respect to a net loss for any taxable year ending on or after December 31, 1986. Such election, once made for any taxable year, shall be irrevocable for that taxable year.” 86 Ill. Adm. Code § 100.2330.

Taxpayer’s IL-1120 for September, 1994, was originally filed on May 9, 1995. On March 6, 1996, taxpayer filed an amended U.S. Corporation Income Tax Return for September, 1994, reflecting a net loss of \$298,797. On March 5, 1996, taxpayer filed an IL-1120 for tax year ending

September, 1995. On this IL-1120, taxpayer showed a net loss for tax year ending September, 1994, of \$298,797 and a carry forward of \$13,480 to tax year ending September, 1995. Taxpayer attached a "Schedule NLD Illinois Net Loss Deduction" to the September, 1995, IL-1120. Part I, Line 2 of the Schedule calls for "Total amount of Illinois net loss previously carried back or forward." Taxpayer provided the amount of \$41,027. Part III of the Schedule requires the taxpayer to "(w)rite the carry year and the dollar amount of the previously used Illinois net loss." Taxpayer provided the following: 9/91 \$11,149; 9/92 \$25,264; 9/93 \$4,614. (Total=\$41,027).

Taxpayer argues that he did not elect to relinquish the right to carry back his losses because on the September, 1995, return, he showed that he was carrying the loss back to 1991, 1992, and 1993. The problem with the taxpayer's argument is that at the time the September, 1995, return was filed on March 5, 1996, the taxpayer had not yet filed amended returns for 1991, 1992 and 1993. Taxpayer stated at the hearing: "The returns were actually done, the amended returns. It just wasn't physically filed." Tr. p. 41. These returns, carrying back the net losses, were not filed until August 5, 1996. So whereas the September, 1995, return required the taxpayer to provide the amounts "previously carried back" and "previously used," in fact, no amounts had been carried back or used at that time. Accordingly, when the Department processed the taxpayer's September, 1995, return, no amended returns carrying back the losses to 1991, 1992, and 1993 had been filed. The Department considered this to be taxpayer's election to relinquish the right to carry back the losses and the election to carry forward only. This election was irrevocable. I have concluded that the Department's position is reasonable and correct here, and the taxpayer's filing of the September, 1995, return without having filed the previously amended returns for 1991, 1992, and 1993, was a relinquishment of the right to carry back.

The amendment to the 1994 federal income tax return was not finalized until May 21, 1996, when the U.S. issued a refund check to the taxpayer for \$4,814.09. Taxpayer next argues that the amended returns for 1991, 1992, and 1993, carrying back the losses, were not filed until August 5, 1996, because the taxpayer was waiting for finalization of the 1994 amendment. The Illinois Income Tax Act requires that the Department be notified of any federal change, in the form of an amended return, not later than 120 days after an amendment has been agreed to or finally determined for federal income tax purposes or any federal income tax refund has been paid, whichever shall occur first. 35 ILCS 5/503. Taxpayer argues that he filed the amended returns for 1991, 1992, and 1993 within 120 days after receiving the federal refund, and this shows his election to carry back the losses.

The problem with this argument is that the 1995 return had already been filed, utilizing a loss carry forward that had also not yet been accepted or finalized by the U.S. After the 1994 refund check was received by the taxpayer on May 21, 1996, the taxpayer did not notify the Department that the 1995 return containing the loss carry forward was not based on a final federal change. Taxpayer zeroed out his tax liability for 1995, with a loss carry forward that was not finalized until 2 months after the return was filed. Taxpayer argues that he did not make an irrevocable election to carry forward on the 1995 return, because the federal change was not finalized at the time the 1995 return was filed. However, the taxpayer never notified the Department that the 1995 return was not based on final figures, and never filed an amended 1995 return. Without notification that the 1995 return was not based on final figures, the Department processed the 1995 return, and the election to carry forward, as if it were a final return.

WHEREFORE, for the reasons stated above, it is my recommendation that the NOD should be finalized as issued.

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Date: May 15, 2000

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Kenneth Galvin  
Administrative Law Judge